

## Proxy Access & Shareholder Proposals

### Developments and Trends for 2012 Proxy Season

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## Proxy Access – A (Brief) History

- Longstanding view among certain groups that shareholders have been denied effective access to the ballot with respect to election of directors
- SEC promulgated proposed proxy access rules in 2003 and 2007; neither was adopted
- 2009 proposal was ultimately adopted, but then vacated
- Battle lines have been essentially the same
  - Business groups have objected to the effect that dissident directors may have on boards; special interest issues; and cost of opposition
  - Shareholder activists focus on fundamental franchise rights of shareholders and a perceived positive impact on Board accountability

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## Rule 14a-11, As Adopted

- As adopted in August 2010, required inclusion in public company proxies of candidates nominated by shareholders in accordance with the eligibility parameters of the rule
- Designed to address concerns that public company boards are not sufficiently accountable to their shareholders
- Eligibility parameters
  - Size/continuity requirement for nominating stockholder(s)
    - *Must have continuously held ≥3% of voting stock for at least 3 years*
    - *Must agree to hold the shares through date of meeting*
    - *Stockholders may aggregate to get to 3%*

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**Rule 14a-11, As Adopted** (continued)

- Shareholders may nominate candidates for up to 25% of the board seats (rounded down), with a minimum of one candidate
- Nomination may not have purpose of change of control
- Vacated by U.S. Court of Appeals for the D.C. Circuit in July 2011

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**Specific Feedback on Proxy Access Rule During Comment Period**

- **Cost/Economic Damage**
  - Commentators believe that boards would, either by choice or by virtue of being compelled by fiduciary duty concerns, expend substantial time and money opposing nominees
  - Some commentators believed that seating shareholder nominate directors harms company performance
- **Special Interests**
  - Concerns that many nominating shareholder may have interests that are detached from those of many other shareholders, and that may be motivated by concerns other than the company's financial performance
- **Alternatives proposed in comments**
  - Allow for shareholders to use Rule 14a-8 process to effect private ordering

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**SEC Adopts Rules**

- SEC adopted Rule 14a-11 by a 3-2 vote in August 2010
  - Dissents were largely based on a perceived lack of data and a perception that the SEC had adopted the rules as a response to political pressure

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**DC Circuit Case**

- Filed by Business Roundtable and Chamber of Commerce after adoption of rules
- SEC stayed Rule 14a-11 (and Rule 14a-8, though that was not part of the case)
- Ultimately, D.C. Circuit vacated Rule 14a-11
- “[We] hold the Commission acted arbitrarily and capriciously for having failed once again – as it did most recently in *American Equity Investment Life Insurance Company v. SEC*, and before that in *Chamber of Commerce* – adequately to assess the economic effects of a new rule.”
- “[T]he Commission inconsistently and opportunistically framed the costs and benefits of the rule; failed adequately to quantify the certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgments; contradicted itself; and failed to respond to substantial problems raised by commenters.”
- SEC announces in September 2011 that it would not appeal DC Circuit decision

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**Rule 14a-8 Amendment**

- Existing shareholder proposal rule amended so that eligible shareholders can cause public companies to include in their proxies proposals regarding the inclusion of proxy access procedures in the company's constituent documents
- Also stayed by DC Circuit, but now in effect for 2012 proxy season

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**Rule 14a-8 Amendment (continued)**

- Grounds for Exclusion (Rule 14a-8(i)(8)) Narrowed
  - Cannot disqualify other nominee
  - Cannot remove director before term expires
  - Cannot question competence, business judgment or character of other nominee
  - Cannot seek to include specific individual in company's proxy materials
  - Cannot affect outcome of the upcoming Board election
  - Other Rule 14a-8(i) grounds for exclusion are available

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### What to Expect and How to Prepare for a Private Ordering Proposal

- Shareholder proposals on private ordering are expected, but not clear how many will be submitted this year and what kind/size of company will be the most common target
- Norges Bank Investment Management (NBIM), manager of the Norwegian Government Pension Fund, has announced the filing of proposals at Wells Fargo, Charles Schwab, Western Union, Staples, Pioneer Natural Resources and CME Group, asking company to establish procedures for shareholders to nominate candidates to the board. Suggested procedures would require that shareholders own  $\geq 1\%$  of company's stock for  $\geq 1$  year and allow up to 25% of board to be nominated by shareholders.
- Rule 14a-8 proposals are limited to 500 words; therefore, private ordering proposals may be more advisory in nature than specific
- Confirm that advance notice bylaws are up to date; brief Board

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### Responding to a Private Ordering Proposal

- Delaware has specific statute (adopted 2009) allowing private ordering bylaws; other states also generally allow
- Proactive adoption?
  - Review bylaws, consider implications of adoption
  - Allows imposition of company-tailored eligibility parameters and director qualification requirements
- Response –
  - Include in proxy and oppose
  - Negotiate for withdrawal
  - Adopt private ordering bylaw and claim substantial implementation exclusion
  - Propose private ordering bylaw and claim conflicting proposal exclusion

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### ISS View on Proxy Access

- 2012 Policy: "ISS supports proxy access as an important shareholder right, one that is complementary to other best-practice corporate governance features. However, in the absence of a uniform standard, proposals to enact proxy access may vary widely; as such, ISS is not setting forth specific parameters at this time and will take a case-by-case approach in evaluating these proposals."
- CASE-BY-CASE approach takes into account, among other factors:
  - Company-specific factors; and
  - Proposal-specific factors, including:
    - Proposed ownership thresholds (i.e., percentage and duration)
    - Maximum proportion of directors that may be nominated
    - Method of determining which nominations should appear on the ballot if multiple shareholders submit nominations.

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Other Shareholder Proposals
<ul style="list-style-type: none"><li>• Majority Voting</li><li>• Anti-Poison Pill</li><li>• Board Declassification</li><li>• Social (e.g., water/environmental; board diversity)</li></ul> <p data-bbox="613 659 756 699">Morgan Lewis</p>

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